Greeks behaving badly?
The micro-origins of crisis and revival

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I feel deeply honored to be delivering the Stavros Niarchos Foundation Lecture this year. But I also feel slightly out of place and out of time as I speak. I will be presenting ideas that have been developed over several years about what is specifically Greek in this crisis. Yet by now every country in the European Union is threatened. Events of historic importance are taking place in the space of just a few weeks. What happens on Friday at the EU summit may have a huge impact on the global economy for the next ten years. Yet here I am, talking about one small country, and how it is different from some of its neighbors.

Still, I will defend the need to understand the local. I have metaphor to offer, about earthquakes: Global capital markets, which are the transmission mechanism of the crisis, are like the shock waves of earthquakes. National economies are like the different buildings in the path of the wave. Some are well constructed to withstand the shock, and survive with just a few cracks. Others will fall, inflicting great pain on the occupants. And some are like canvas tents, which are barely affected.

Many economists are like seismologists, analysing the big picture that creates the waves. Others are more like civil engineers, trying to understand how different local structures behave, in earthquakes as well as in tranquil times. And some, like me, are the anthropologists of building: why do some people build with wood and others with concrete? When earthquakes strike, naturally the news is full of seismology. But later, it will be time to build again, and we shall need to re-examine our assumptions about buildings. So, on to the Greek story.
We tend to look at the crisis in Greece, or in any other country, in terms of macroeconomic magnitudes: GDP and debt and so on. But behind these numbers, there are specific goods and services that are produced and traded. And behind the goods and services, there are people in households and in firms, who decide to work in particular ways and to consume and to invest. And behind the people, there are institutions that enable or hinder their actions. And the people also have prevailing mentalities, or in other words a culture, that guide them in economic behavior.

The diagram illustrates this, to help you keep track of where we are in the lecture. I am going to focus on the three items on the left, that is, on what goes on behind the numbers, and the sectors. What happens there, in my view, can explain most of the difference in how different countries perform in terms of GDP, trade, deficits, and so on.
First, though, about the macro-magnitudes. The broad story is well-known: the Greek state became insolvent before any other EU country, because it had by far the worst combination of four magnitudes: Government deficits over many years; government debt (which is a stock figure, deriving from the flow of deficits); trade deficit; and savings rate. It is the combination of the four that made Greece the sick man of Europe, much more than any other country in the European periphery.

Most of the discussion in Greece has been about the first two figures: the government deficit, which must turn into a surplus soon, because nobody is willing to finance it anymore. And the debt, which is now so high, that nobody believes it can ever be repaid in full. Roughly speaking, eliminating the deficit is the hard work that the Greek state must do. And writing off much of the sovereign debt in an orderly way is the hard work that global and European institutions must do. Both of these issues are directly political and highly controversial; so they have hogged the limelight.

But on a more fundamental level, it is the high trade deficit and the low savings rate that matter more. These were persistently, over many years up to 2009, the highest and lowest in Europe respectively. I will not dwell on the numbers here. I am more interested in exploring why the numbers happened. Why is Greece a deficit country, both in government and in trade?
The next level is to look at the sectoral composition of activity. What services and products do Greeks produce and consume? This will reveal structural weaknesses in the economy that will not be remedied by fiscal policy or by high-level negotiations with creditors. In Greece, this weakness is encapsulated in the popular phrase: “the frappe economy” (frappe being our national daytime drink: cold, shaken, instant coffee). It refers to low-value added, easy to provide services, related to leisure and to location, and to tourism, of course. This is not a very accurate picture of the economy, but it does contain a lot of truth.

In broad terms, over the past thirty years Greece has tilted too much towards nonmarket public services, and towards marketed private services that are not however tradable internationally (like retail shops, lawyers, doctors and hairdressers). I will have some more to say on the sectoral composition later, but for the moment let us try to explain why this happened.

This is the part where Greeks specifics come into play.
Look at how production is organized, first. Greece is an extreme outlier in terms of the number of self-employed and of small businesses.

Greece has the most people employed in units of under 10 people among the 27 EU countries

Source: Eurostat, Statistics in Focus, 31/2008
In the so-called ‘non-financial business economy’ (NFBE) 57% of those employed are either self-employed or employed in firms of under 10 employees. The value of this index for EU-27 is 30%. Italy comes second with 47%, Portugal third with 42%. France is at 27%, the UK at 21%, Germany at 18%. (2007)

![Self-employment as % of civilian employment, 2008](image)

In the economy as a whole, (which includes agriculture on the one hand, but also banks and government on the other) 35% of the labor force is self-employed, or unpaid family members. This is by far the highest figure in the EU, but also the second highest in the OECD, after Turkey. In the US the corresponding number is 7%, in Germany 12% and in Italy 26%, and in all of the OECD 16% (2007).
You may well ask, why? How did it happen that we have so many small businesses – vineyards, olive presses, rooms-to-let, mini markets, doctors’ practices, theaters, clothes boutiques, clothes makers, IT workshops – and why so few large employers?

The short answer is that we owe it first, to history, and more specifically to the Ottoman state, which prevented primitive accumulation of capital as it occurred in the west; second, to the institutions of our modern state, which assist the survival of small business but make it hard for them to grow into large enterprises; and third to our culture which makes it hard for us to cooperate.

Institutional bias in favor of the small scale has been so strong since the beginning of the modern Greek state, that neither the 1.5 million of incoming Greek refugees in 1922, nor the huge wave of poor immigrants since 1990 became a permanent proletariat for big employers, as has happened elsewhere. It was small employers who became rich in farms and in building sites on the back of the immigrants.

I believe that self-employment, micro-employment and family business is a stable and fundamental institution in our economy, perhaps the most fundamental. Their share in employment and output will not shrink under normal circumstances. Not even a long and deep recession will change this. Only a revolution in institutions would.

If that is so, we should accept the following: it is institution that determines specialization, not the other way around. That is: because we are a society of small business, we do not build electronic devices; rather than: because we don’t produce such devices we have small businesses. This insight often escapes policy makers. They believe that with the right funding and infrastructure we may grow competitive businesses in industries that require a larger scale. In every era, small
businesspeople will do the work that suits them. Yesterday diving for sponges, today letting rooms to tourists, tomorrow what?

Family strategies are distinctive in this small ownership environment, and quite different from what you might find in most of the western world.

The family will seek stability in polyergy (a term coined by G. Dertilis): having varied sources of income, as many as it can find and appropriate. There is family solidarity: multiple incomes require multiple hands. The father has a petrol station, the son studies information technology for the upside, but if it doesn’t work out he will not starve. The daughter preferably becomes a teacher or a municipal clerk – something secure which leaves free time to care for elderly parents and for the next generation. If the family shop does well, the whole family will work there; if not it will be maintained by one or two members. The system is admirably stable, flexible and long-lasting.

In a small-ownership economy household saving and investment is also different. It is channeled, quite rationally, into real estate and into education. In western economies savings are invested collectively through pension funds, mutual funds and bank deposits. They end up funding industry, technology, infrastructure, and in general, sizeable organizations. In the Greek micro-economy monetary savings have few reliable collective outlets.

Human capital takes a different form. In western economies human capital can develop in standardized career paths – that is, by building relationships inside organizations. Higher education is useful mostly as a first step in a career – if the jobs market does not demand it, the young will not insist on getting it. In small ownership, the value of a person is vested in their individual characteristics. The jobs market does not give clear signals. I want an engineering degree not in order to work at Volkswagen, but because I will have numerous options, as a reseller, contractor, consultant, retailer or just possibly a middle manager. That is why families overinvest in education for the young: in English language tutorial schools, in university exam tutorial schools, in living expenses for out-of-town studies, and even for studies abroad. In national accounts these expenses appear as consumption, but they are investment.
Moving beyond firms and households, to the institutions that appropriate resources and that regulate the economy: next distinctive characteristic in Greece is the wide prevalence of rents, most of which are conferred via the political system. Note that I define rents a bit differently from the standard economic definition. In broad terms it is unearned income which derives from privileged access to a scarce resource. The operational term is ‘privileged’, i.e. a particular, special income, that is not available to the population as a whole. For example, if a country provides for a basic pension for all citizens over the age of 65, this may be unearned income, but it is not a privilege: it is based on a simple and general rule which applies to a big category of citizens. I would not call that a rent. If, however, as is the case in Greece, some professionals get higher pensions at an earlier age, just by warrant of belonging to a particular occupation, this is rent.

Politically conferred rents are the result of clientelist politics, i.e. of the politics of the particular rather than the general. They come in many forms: sinecures in the public sector, privileged pensions, investment subsidies without any impact on development, extraordinary profits of government contractors, and graft. They also derive from regulations which allow some people to overcharge in the market (restricted professions, regulated prices, prohibitions), and, less obviously, to the benefits of breaking the law when your competitors are conforming. In this context, corruption in the sense of taking bribes is just a special case of rent harvesting, which in most other cases is legal.

It is important to note that rents are widely and democratically distributed. Especially after 1980, most households could get some benefits from the system. Democratic legitimacy was strengthened by new institutions that made access to rents more impartial: the state started hiring based on standardized examinations
ASEP, and the university entrance mechanism eliminated the possibility of personal favors. If people have to work hard and to compete honestly in order to gain access to a position, nobody questions whether the position itself is parasitical. And the privileges attached are considered fair.

There are also substantial non-political rents in the private sector. Tourism income includes a major rent component, since visitors pay first for location and then for service. Transfers from ships and emigrants are the fruit of real work abroad, but for the receiving local economies they act as pure rent.

So rent appropriation mechanisms are quite varied, but they have a common effect on economic culture: almost all Greeks, from large business owners to small landowners in islands and to municipal clerks in villages, believe it is natural to have some income which derives neither from work nor from risking capital. If they cannot have it, they feel wronged.

The dominance of rents, or rentocracy, will shape politics and administration and culture. To name just the most important effects briefly: It fosters a Zero-sum mentality: rent does not contribute to growth, it only shares in what is there. It breeds populism, whose fundamental strategy is to shift responsibility for the whole to the opposite pole, the enemy. We, the people, fight for our share of the pie, it is others who are responsible for the size of the pie.

Rentocracy also abhors measurement: rentiers do not need to measure the world; producers do. Rentiers will haggle. Producers will plan inputs and outputs and will try to maximize the margin between the two. The rentocratic state behaves like the rentier. It bargains constantly with various groups, and always gives a little more than it started out to. It is not constrained by an absolute limit for expenditure. It ends up invariably in deficit, which had not been planned.

Beyond fiscal numbers, society in general does not demand measurements, either for pollution, or for the quality of hospital care, or for the impact of policing on crime. There is no pressure on public services to count and to evaluate. That is how we get to ‘Greek statistics’, long before anybody intentionally tampers with the numbers.
On to culture. A lot of talk in Europe and in Greece is about the mentality of Greeks, which is somehow different from most western people, and which lies at the root of behaviors such as corruption or excessive consumption. I think there is truth in this, but not in ways that are usually discussed. I disagree that Greeks are lazier than others. And I disagree that our economic culture is in some sense a vestige from the past, i.e. that we have not embraced modern rationality. I think that a fundamental aspect of our economic culture is opportunism, and this is a rational and modern trait, albeit short-sighted. I refer to opportunism in the game-theoretic sense: a tendency to break rules, or to defect, if that will lead to tangible short-term gain.

We are a society of low trust and of low social capital; this is borne out by several cross-country surveys, such as the World Values Survey. It is also common experience, when you do business: in venture capital, in which I’ve worked, trust and cooperation between founders and investors is a major problem. Many deals have failed because the parties had different agendas. I have compared notes with colleagues from northern Europe, and there are a lot of things that they can take for granted, which we in Greece could not – starting from basic reporting of facts and numbers.

I have often asked myself, why this difference? My tentative explanation is that over several centuries Greeks missed out on two fundamental processes that can foster cooperation among strangers. One lies in the domain of anthropology: the process by which the Western person has internalized, or “individualized”, the rules of society. The Catholic Church and later the Protestant movements have been instrumental in this. The Greek Orthodox church, with its emphasis on the mystic and the hereafter, took a different route.
The second process lies in politics and economics, and it has to do with building and reproducing hierarchies, which impose rules from above. In the West, feudalism, monarchy and the Catholic Church interacted to create the absolutist state which was mandated to rule and guide society. The bourgeoisie inherited this state and reinforced its role of societal guidance. In parallel, during the industrial revolution large business hierarchies were developed, which assigned stable positions to workers and clerks. Such things did not happen in Greece: we overthrew the Ottoman state rather than developing it, and we resisted economic hierarchies.

In other words, advanced western economies were founded not only on free markets and individual incentives. They were founded on hierarchies (vertical rules) and on strategies of cooperation (horizontal rules). Successful and hegemonic capitalism is free markets embedded in a society of rules and responsibility. Otherwise, it is either a jungle, or a community of corner shops. We Greeks have subscribed neither to vertical nor to horizontal rules. We are neither obedient nor cooperative. If we have avoided the jungle, Russia style, is because we have kept the corner shops.

So we may not be good at governing the commons, but we have developed some admirable economic institutions for dealing with opportunism, which western technocrats find peculiar. Take post-dated cheques, as a means of trade credit. Each party is responsible for the counterparties they choose. Name and reputation count. It is remarkable that no recipient of these cheques will try to cash them before their designated dates, even though legally they could do so. If they do, they will be effectively expelled from the market. The legal framework that supports the system is also quite efficient and predictable, uncommonly so for Greece. It reinforces trust among transacting parties because it carries immediate sanctions for an issuer who cannot cover the cheque, without involving the bureaucracy of banks as intermediaries. This is an institution of peer-to-peer credit, which developed spontaneously from below and is based on personal responsibility. We should be fostering such institutions, not be thinking how to banish them.

Opportunists are not inherently crooks. They are ‘rational egoists’. They will conform to rules if they think it is in their interest. In an environment where most people are cooperators and where opportunism is punished, opportunists turn into cooperators. Greeks get can work very well within American institutions, once they are sure that everyone else also plays by the rules. But if opportunists are a majority, to begin with, it is very difficult for the group to converge towards cooperative behavior. The issue here is path dependence. In this context, I think that Greek opportunism can be turned into an asset in the future global economy. More on that later.
Let us see now how small ownership and rent appropriation combine in the big picture. To do this, we’ll go back to the sectoral composition of the economy. One fundamental distinction is between tradable and non-tradable industries.

**NON-TRADABLE**
- Government
- Utilities
- Banks (commercial)
- Telecoms
- Media
- Retail
- Building
- Shops
- Lawyers
- Hairdressers

**TRADABLE**
- Manufacturing
- Airlines
- Shipping
- Tourism
- Agriculture
- Workshops
- Digital Applications
Here is an indicative list. On the left are activities which by their nature cannot be provided from afar, and are not subject, therefore, to international competition. On the right, tradable goods and services, that compete in global markets.

Another distinction has to do with size and organization. Some activities, such as public administration or telecoms are delivered by large hierarchies with many employees. Others, such as hairdressers, in small shops. In between there is a whole spectrum; in furniture, one can find around the globe the whole gamut, from one-man shops to firms with thousands of employees; the same true for accountants.

The reason I am putting up this diagram is that each of the four quadrants operates under a different set of constraints, institutions and regulations. I’ll talk about that in a moment, but some numbers first.
This is how the labor force was distributed in the four quadrants in 2007. If we go back to 1992, the tradable sectors accounted for about 38% of all employment; in 2007 that had dropped by 13 points to 25%. These 15 years saw a massive shift of resources from the right hand to the left hand column. Now a shift to non-tradables is a common pattern in most post-industrial economies, but there are different routes by which this happens. In Greece the shift was excessive, as witnessed in the very high and persistent trade deficits, over many years. The trade deficit was financed by government borrowing. This created excessive domestic demand, which tilted the balance to nontradables.

But, and this is very important, the effects of politics went far beyond an excess of demand. By regulation and by rent creation, they shaped an institutional framework that encouraged people and firms to move away from anything that was exposed to global competition, to the cozy world of lifetime employment and protected professions.

Take the upper left hand, i.e. the organized, hierarchical, non-tradable group. Government, banks (retail banks), telecoms, public works contractors. Here competitive pressures are negligible, and employment protection has been high. Most Greek labor legislation, as well as pensions and social benefits, were shaped by the corporatist bargains and constraints within this quadrant; these then spilled over to the rest of the economy, where they were neither viable nor enforceable.

The bottom left quadrant is the domain of the self-employed professional and of the family shop. Many of the activities here were regulated in ways which restrict competition, and/or were supported with generous pension schemes; especially the white collar, university-degree trades (lawyers, pharmacists, engineers). Others grew
without special protection, on the basis of family strategies of upward mobility. There are tens of thousands of excess doctors, teachers, etc, either active or in-waiting. To survive, doctors have created excess demand for their trade, and teachers or nurses have exploited the weakness of public services to set up complementary private services. Having provided an alternative, they have also lifted the pressure for public services to improve. Others had no special privileges (building tradesmen, restaurant owners, shopkeepers), but they were able to remain independent because of the institutional bias against large companies; and they were able to make a living, because of the demand generated by the twin deficits.

The picture is very different in the tradable industries. Here the state cannot provide much protection or rents to businesses. This is forbidden by the rules of the EU and the World Trade Organization.

In the bottom right hand quadrant there are about one million jobs. About half are in agriculture, about 30% are in manufacturing, and the rest are in services. In so-called ‘manufacturing’ most of the jobs are in workshops: bakeries, carpenters and ironmongers, seamstresses. In services, they are in tourism. Institutional protection is limited. It has been substantial for parts of the agricultural sector, via the Common Agricultural Policy, i.e. for farmers who grow wheat or cotton in central and northern Greece; but not for producers of fruit and vegetables. Most of the quadrant survives on a mix of skill, hard work, and by the weak protection afforded by distance from the efficient large competitor. Tourism and many of the farms also rely on natural advantage.

These are entrepreneurial occupations. They have to respond to changes in technology and competition, they are directly affected by globalization, they do not turn to the state for subsidies and regulation, they must manage cash flow, and in some cases they also hire and fire. At the same time, they have lower social status than the protected professions in nontradable lower quadrant.

One factor in survival is low compliance to regulation. But low compliance has a price: they must keep below the radar by keeping small. The transition from self-employment to being an employer is especially tricky: if they can hire without paying all the non-wage costs, it can be profitable; if they abide by all the rules, it may not be. For these businesses, the large influx of immigrants since 1990 has been a bonanza.

Finally there is the quadrant of organized, sizeable companies that compete in the world market. As you can see, it is minute. 2.5% of total employment, by the official definition of a big company of 250 employees or more. Even if we stretch that definition to include all firms with more than 20 employees, the quadrant is just 6.5%.

To make a long story very short, this is because regulation spills over from the cosseted large nontradable quadrant to this one, which has to compete against foreigners. And because small firms have an informal advantage in being able not to comply with regulation. And because there is a general ideological and institutional bias against capitalist production. And because salaries in the public sector grew much faster than the private competitive sector could afford. In summary, the most
attractive career paths, the better business opportunities and the highest margins were all in the non-tradables.

Steady growth can only resume if there is a large shift of resources back to tradables, into new viable competitive businesses. In terms of jobs this shift may have to be about 15% of total employment. That is, 750 thousand people will have to move into different activities from where they were in 2008.

How can this be done? This complicated diagram illustrates the various paths by which new jobs may be created. The arrows on top pointing down are foreign direct investment, the one on the top right pointing up is growth by large domestic firms, and so on.

The point of drawing these paths is the following: each of the arrows reflects a specific type of shift of resources, which involves different types of actor, different policies and different human consequences. This one, (upper right hand) for example, is about existing firms that have excess capacity because of the downturn, and can easily expand their business if demand picks up; or if, by devaluation, they gain a cost advantage. In a good scenario, they may also invest in additional plant. Here, the business model exists, and so does the management team. They will just hire more employees, who will move easily into jobs that are waiting for them.

This transition (lower middle) however, from a small nontradable business into a new tradable one, involves people risking a move into a new job that they will have to create from scratch. It involves, for example, a doctor who has spent a dozen years becoming qualified now deciding to start a small export business. There will be a sense of failure, of dislocation, of great risk before and during that move. It is not just a change of jobs, it is a change of identity.
Policy makers and economists tend to focus on the paths with the red arrows, i.e. on foreign direct investment and on the expansion of existing, sizeable players. My view is that in the case of Greece these can have very limited impact. It is the green arrows that we should be trying to encourage, by any means possible. That is, the rapid creation and growth of tradable micro-businesses. This is not a standard model of export-led growth, but then Greece is not a standard economy in this respect. We will have to invent a model based on wide ownership, polyergy and the small scale. This is where our institutional comparative advantage lies.

**Micro-origins of the revival**

So, going back to the broad analysis, what must we keep, and what must we change?

The small scale is, I believe, exogenous; a constraint. Of course, we should have an environment which enables small firms to grow into big ones, and we should do this mostly by leveling the playing field of compliance. But it is mainly the outlook and the strategy of the small firms themselves that should change. Can they transform their offering? Can they become more competitive?

Families have important assets in trying to build new businesses: Ownership, and experience with multi-tasking, and investment in education. So there is a solid foundation there. Bureaucracy and regulation are big barriers today, but governments can remove these if they decide to do so. This can mean real cost savings quickly.

What about rents in the non-tradable economy, which distort incentives for entrepreneurs, and which impose heavy costs on everybody? This is where the crisis becomes an opportunity. Fiscal constraints are making it very difficult for the state to continue to award incomes to special groups. Those rents that have a direct fiscal cost are already being cut. Those that derive from regulation, such as closed
professions, could survive in the crisis, of course. The troika is pressing to remove them, and there seems to be majority of public opinion for liberalization. But change is by no means certain, and the political struggle around this will continue.

What if Greece were to quit the eurozone, how would this affect the shift to tradables? Economists who are not very familiar with the Greek situation, often say that it would be a great help. In terms the immediate impact on relative unit costs, this is true of course. But for this to lead to a sustained growth of exports other things must happen as well. Entrepreneurial energy and capital must flow into new businesses in the uncertain world of global competition. This will not happen if the state is able to print money and to run deficits that will continue to finance cozy privileges. So, as the eurozone is at last starting to impose some sort of order on the Greek rentocratic system, exit would give a second wind to it. Rents are the main reason why we should avoid the drachma.

Finally, on opportunism.

At the start of my talk, I defended the need to understand the local. To end, I will offer some thoughts on how this particular local may help us think about the global. Greek opportunism, I believe, is the normal behaviour of the homo economicus, the ‘rational egoist’; the opportunist defects in the absence of strong enforcement of rules. In many other western societies, people are not rational egoists, they are more cooperative by pre-disposition. They are, in the words of Elinor Ostrom, “conditional cooperators”. But the foundations of that predisposition may be eroding. In postmodern societies collectivities become fluid, identities are shifting, uncertainty is increasing, along with individual choice. It is the world of Ulrich Beck's do-it-yourself biographies, and of Richard Sennet’s culture of the new capitalism. Hierarchies are
losing their control over the self-interest of the individual and internalized rules of cooperation are dissolving. If this is so, then Greek opportunism may be a glimpse of the future of the West.

Will this be a dystopic future? Maybe yes, maybe no. It will pay to observe how Greeks, who did manage to build a good life in the past 30 years, will cope with this crisis. The news is not all bad. Hardship has brought anger and conflict. But it has also brought out new civic initiatives, as people realise that the paternalistic state cannot deliver anymore.

Teachers stay on after school, to help pupils in need, voluntarily. Guerilla gardeners are cleaning up the cities. Farmers are forming new cooperatives. These are not mass movements, but they do show how individuals are rediscovering the benefits, and even the pleasures, of solidarity under pressure.

On another level, global markets and technology are creating a new framework for stable cooperation among opportunists. The web and social media, common standards, and workflow management tools, render each person’s contribution transparent, and can make much of hierarchy redundant. Individuals or small teams can have a global presence and global reputation. A lone programmer is now able sell her services all over the world. For the first time in history, goods can be produced collectively and responsibility apportioned individually. These are tools of cooperation for opportunists. Beyond business, they can leverage small amounts of voluntary work into major contributions to collective welfare (as in Wikipedia), and can allow the maintenance of some collective goods without asking for big personal sacrifices. Could it be that Greek individualism can now find a creative role in the world economy?

It can happen; but to build a whole new national economy around such small scale endeavors, there will have to be a connecting tissue: institutions that support the individuals, and most importantly, a new public narrative. Greece will be a testing ground for shaping a new narrative out of the rubble of a failed model.

What could be the building blocks for that? Perhaps it will be common role models. Perhaps clusters of similar businesses, and networks of peer-to-peer learning. Perhaps it will be public services with equal access for all at a good minimum standard. Perhaps a new respect for the commons, based on information and transparency and individual responsibility. Perhaps new models of local democracy. I believe and hope that it will be most or all of these. But I may be very wrong.

So, watch this space and find out.